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No. 14-1132

IN THE

Supreme Court of the United States

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC., ET AL.,

Petitioners,

v.

GREG MANNING, ET AL.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

BRIEF OF NASDAQ, INC., NASDAQ STOCK MARKET LLC, NEW YORK STOCK EXCHANGE LLC, NYSE ARCA, INC., AND NYSE MKT LLC, *AS AMICI CURIAE* IN SUPPORT OF PETITIONERS

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TABLE OF CONTENTS

Page

INTEREST OF *AMICI CURIAE* 1

STATUTORY PROVISION INVOLVED 3

SUMMARY OF ARGUMENT 3

ARGUMENT 6

I. SECTION 27 OF THE EXCHANGE ACT IS A BROAD GRANT OF EXCLUSIVE FEDERAL JURISDICTION 7

II. EXCLUSIVE FEDERAL JURISDICTION IS NECESSARY FOR EFFICIENT FUNCTIONING AND EFFECTIVE REGULATION OF THE NATION'S SECURITIES MARKETS 12

A. SROs PLAY A KEY ROLE IN SECURITIES TRADING AND REGULATION 13

B. EXCLUSIVE FEDERAL JURISDICTION PROVIDES UNIFORMITY THAT IS NECESSARY FOR SROs TO FUNCTION EFFECTIVELY 16

III. THE SECOND CIRCUIT'S MORE RECENT OPINIONS HAVE CALLED INTO QUESTION ITS ERRONEOUS DECISION IN *BARBARA* V. *NEW YORK STOCK EXCHANGE* 21

CONCLUSION 28

TABLE OF AUTHORITIES

Page(s)

CASES

Altman v. *SEC*,
687 F.3d 44 (2d Cir. 2012) 17, 18, 20

Barbara v. *NYSE*,
99 F.3d 49 (2d Cir. 1996) ..... *passim*

Bonito Boats, Inc. v. *Thunder Craft Boats, Inc.*,
489 U.S. 141 (1989) 12

Brown v. *Pro Football, Inc.*,
518 U.S. 231 (1996) 19, 20

Credit Suisse First Boston Corp. v. *Grunwald*,
400 F.3d 1119 (9th Cir. 2005) 15

Credit Suisse Sec. (USA) LLC v. *Billing*,
551 U.S. 264 (2007) 19

D'Alessio v. *NYSE*,
258 F.3d 93 (2d Cir. 2001) 24, 25

DL Capital Group v. *NASDAQ Stock Market*,
409 F.3d 93 (2d Cir. 2005) 13, 17

Grable & Sons Metal Prods., Inc. v. *Darue Eng'g & Mfg.*,
545 U.S. 308 (2005) 25, 26

Gunn v. *Minton*,
133 S. Ct. 1059 (2013) 26

Hawkins v. *NASD*,
149 F.3d 330 (5th Cir. 1998) ..... *passim*

Hibbard Brown & Co. v. *NASD*, No. 94-285,
1994 WL 827778 (D. Del. Oct. 6, 1994) 10

Lowe v. *NASD Regulation*, No. 99-1751,
1999 WL 1680653 (D.D.C. Dec. 14, 1999) 10

Matsushita Elec. Indus. Co. v. *Epstein*,
516 U.S. 367 (1996) 13

NASDAQ OMX Group v. *UBS Secs., LLC*,
770 F.3d 1010 (2d Cir. 2014) 25, 26, 27

In re NYSE Specialists Sec. Litig.,
503 F.3d 89 (2d Cir. 2007) 10

Platinum Partners Value Arbitrage Fund, Ltd. P'ship v. *Chi. Bd. Options Exch.*,
976 N.E.2d 415 (Ill. Ct. App. 2012) 19

Rogers' Estate v. *Helvering*,
320 U.S. 410 (1943) 12

In re Series 7 Broker Qualification Exam Scoring Litig.,
548 F.3d 110 (D.C. Cir. 2008) 13, 17, 20

Shearson/Am. Express Inc. v. *McMahon*,
482 U.S. 220 (1987) 15

Sparta Surgical Corp. v. *NASD*,
159 F.3d 1209 (9th Cir. 1998) ..... *passim*

Swirsky v. *NASD*,
124 F.3d 59 (1st Cir. 1997) 13

United States v. *Locke*,
529 U.S. 89 (2000) 12

United States v. *NASD*,
422 U.S. 694 (1975) 20

CONSTITUTIONAL PROVISION

U.S. Const. amend. V 22

STATUTES

15 U.S.C. § 77v 8, 9

15 U.S.C. § 78c 1

15 U.S.C. § 78f 2, 15, 16

15 U.S.C. § 78o-3 15

15 U.S.C. § 78s ..... *passim*

15 U.S.C. § 78y 20, 23

15 U.S.C. § 78aa ..... *passim*

28 U.S.C. § 1331 ..... 9, 22, 23, 26

42 U.S.C. § 1983 22

Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74 9

RULE

S. Ct. R. 37.6 1

OTHER AUTHORITIES

Concept Release Concerning Self-Regulation, SEC Release No. 34-50700, 69 Fed. Reg. 71,256 (Dec. 8, 2004) 13, 14, 15

Louis Loss, *The SEC Proxy Rules and State Law*, 73 Harv. L. Rev. 1249 (1960) 21

Market 2000: An Examination of Current Equity Market Developments (Jan. 1994) 14

S. Doc. No. 93-13 (1973) 17

BRIEF OF NASDAQ, INC., NASDAQ STOCK MARKET LLC, NEW YORK STOCK EXCHANGE LLC, NYSE ARCA, INC., AND NYSE MKT LLC, AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF *AMICI CURIAE*

NASDAQ, Inc. and NASDAQ Stock Market LLC (collectively, "NASDAQ") and New York Stock Exchange LLC, NYSE Arca, Inc., and NYSE MKT LLC (collectively, "NYSE") operate the principal stock exchanges in the United States.[1] *Amici*'s exchanges are the global leaders in raising capital for listed companies and have provided a reliable, orderly, and efficient marketplace for securities trading for many decades. As entities directly and comprehensively governed by the Securities Exchange Act of 1934 ("Exchange Act") and the U.S. Securities and Exchange Commission ("SEC"), NASDAQ and NYSE have a keen interest in the Exchange Act's effective and uniform application and interpretation.

NASDAQ and NYSE are registered with the SEC as national securities exchanges under the Exchange Act and are self-regulatory organizations ("SROs") within the meaning of 15 U.S.C. § 78c(a)(26). The Exchange Act both authorizes and requires SROs to adopt and enforce rules governing the conduct of

[1] All parties have consented to the filing of this brief. The written consents have been lodged with the Clerk of the Court. Pursuant to Supreme Court Rule 37.6, *amici* state that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than *amici* and their counsel, made a monetary contribution intended to fund the preparation and submission of this brief.

their members and persons associated with their members, *id.* §§ 78f(b), 78s(g), "to remove impediments to and perfect the mechanism of a free and open market," and "to protect investors and the public interest," *id.* § 78f(b)(5). More generally, the Exchange Act authorizes and requires SROs to adopt and enforce rules governing the operations of their markets. *See ibid.*

Amici have a substantial interest in the uniform application of federal securities law, as envisioned by the Exchange Act. Organized and consistent regulation of SROs under the Exchange Act provides SROs with a coherent, predictable framework so that they can fulfill their regulatory duties as Congress intended, without fear of recriminatory and unpredictable lawsuits in various state courts.

Amici believe that the Exchange Act's grant of exclusive federal jurisdiction for suits involving the Exchange Act or any rules promulgated thereunder—including the SRO rules discussed above—is necessary to promote and maintain the uniform regulatory framework created by Congress. Without exclusive federal jurisdiction, SROs would be exposed to regulation by state courts across the country. If the Third Circuit's view in this case were to prevail, *amici* anticipate a substantial degradation of the consistency, reliability, and predictability of the legal regime that governs SROs, provides consistent application of SRO rules to members and their associated persons, and contributes to the investing public's confidence in the markets. Exposing SROs to litigation under each separate state system is a serious threat to the uniformity that Congress envisioned. The resulting patchwork of regulatory schemes would make it extremely difficult and costly for

SROs like *amici* to perform their congressionally mandated functions, and in turn would undermine the nation's securities markets.

The consequences of the Court's ruling in this case, in other words, will be visited most directly and pervasively on SROs, which are the most frequent litigants in cases involving Section 27. *Amici* therefore possess highly relevant experience regarding how litigation in cases implicating Section 27 affects SROs' effective functioning under the Exchange Act's regulatory system.

STATUTORY PROVISION INVOLVED

Section 27 of the Securities Exchange Act, 15 U.S.C. § 78aa(a), provides in relevant part:

> The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder.

SUMMARY OF ARGUMENT

I. Section 27 of the Exchange Act provides that federal district courts "shall have exclusive jurisdiction" over any lawsuits alleging "violations" of the Act or its regulations, or seeking to "enforce any liability or duty" they create. The provision is an affirmative grant of exclusive jurisdiction, not simply a divestiture of concurrent jurisdiction in the state courts, and its application does not turn on whether

the plaintiff characterizes its claim as arising under state or federal law.

The Third Circuit concluded that Section 27 is not an independent grant of jurisdiction, and that claims falling within its terms may proceed in federal court only if some other basis for jurisdiction applies. But the plain language of the statute—"*shall have* exclusive *jurisdiction*"—confers jurisdiction on the federal courts. That jurisdiction under Section 27 is *also* exclusive does not change this conclusion. Moreover, it is irrelevant whether the plaintiff chooses to characterize its lawsuit as arising under state law. This conclusion is aptly illustrated in cases against SROs, which constitute the overwhelming majority of lawsuits in which Section 27 is litigated. The majority of the decisions to consider the issue have correctly concluded that the purportedly state-law nature of the claims asserted is immaterial provided that they allege "violations" of, or seek to "enforce any liability or duty" created by, the Exchange Act, SEC rules, or SRO rules. *See, e.g.*, *Hawkins* v. *NASD*, 149 F.3d 330 (5th Cir. 1998); *Sparta Surgical Corp.* v. *NASD*, 159 F.3d 1209 (9th Cir. 1998).

II. Section 27 reflects Congress's desire to promote uniformity and predictability in the securities markets by ensuring that the content and application of the Exchange Act and the rules thereunder are determined by federal courts. This goal is particularly important in the SRO context, where permitting state-court litigation against SROs based on alleged violations of the Exchange Act, SEC rules, or SRO rules—or the duties and rights created thereunder—would subject national exchanges to numerous additional regulators and lead to inconsistent interpretations of federal law across the country.

A. The Exchange Act's comprehensive system of federal regulation relies on self-regulation by SROs. SROs promulgate rules governing their members, which are subject to SEC approval, abrogation, or alteration. SROs also conduct investigations and examinations, which are also subject to comprehensive review by the SEC, and are designed to identify and prevent rule violations by their members.

B. Section 27 funnels challenges to SRO actions into the federal court system to ensure that those actions are judged by a uniform federal standard, as applied by the federal courts and the SEC. This uniformity is important because SROs must make innumerable regulatory decisions that potentially affect market participants, and they can do so only with the certainty that their actions will be judged by a consistent federal standard that is consistently applied. In contrast, if state courts were permitted to adjudicate state-law claims resting on the premise that an SRO violated the Exchange Act, SEC rules, or the SRO's own rules, then each state could adopt differing interpretations of those provisions that would effectively impose different requirements from other states and from the uniform federal standard.

II. The Third Circuit reached a contrary conclusion based largely on Second Circuit *dicta* in a decision predating the contrary authority from other courts of appeals. That decision—*Barbara* v. *NYSE*, 99 F.3d 49 (2d Cir. 1996)—did not discuss or analyze the text of Section 27. Rather, it treated that provision as largely coextensive with federal-question jurisdiction (and thus inapplicable to many state-law claims) before upholding jurisdiction on other grounds. In addition to being incorrectly reasoned, *Barbara*'s jurisdictional *dicta* has been undermined

by subsequent Second Circuit decisions, which have upheld jurisdiction under Section 27 on materially indistinguishable facts and, notably, invoked that provision in support of jurisdiction over state-law claims.

ARGUMENT

Section 27 of the Exchange Act provides that "[t]he district courts of the United States . . . shall have exclusive jurisdiction of violations of [the Exchange Act] or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by [the Exchange Act] or the rules and regulations thereunder." 15 U.S.C. § 78aa(a). As Petitioners have explained, this provision is an affirmative grant of exclusive federal jurisdiction to the federal courts, and the Third Circuit erred in concluding otherwise. *See* Pet. Br. 19–23, 28–31.

Amici submit this brief to emphasize the importance of Section 27 to the proper and uniform functioning of the securities markets. By granting exclusive federal jurisdiction over claims involving alleged "violations" of the Exchange Act or the regulations thereunder, or seeking to "enforce any liability or duty" that they create, Congress channeled all litigation in this area—including lawsuits against SROs based on their SEC-approved rules—into the federal system. Any contrary rule would expose SROs to potentially conflicting interpretations of the Exchange Act, the SEC's rules, and SRO rules, and would subject SROs to regulation by the fifty states—rather than a single and uniform system of federal regulation.

Most cases addressing Section 27 have involved SROs, and the majority of these decisions have cor-

rectly concluded that the statute's grant of exclusive federal jurisdiction cannot be dismissed as merely depriving state courts of concurrent jurisdiction. The outlier before this case—a Second Circuit decision relied upon below—was wrongly decided and has been thoroughly undermined even within the Second Circuit itself; it should therefore provide no support for adopting an interpretation of Section 27 that would destroy its critical role in ensuring the uniform federal interpretation of the Exchange Act, including the regulatory system governing SROs.

I. SECTION 27 OF THE EXCHANGE ACT IS A BROAD GRANT OF EXCLUSIVE FEDERAL JURISDICTION.

Section 27 provides that "[t]he district courts of the United States . . . *shall have* exclusive *jurisdiction of violations* of [the Exchange Act] or the rules and regulations thereunder, *and of all suits in equity and actions at law brought to enforce any liability or duty* created by [the Exchange Act] or the rules and regulations thereunder." 15 U.S.C. § 78aa(a) (emphases added). Whenever a lawsuit alleges "violations" of the Exchange Act or its regulations, or seeks to "enforce any liability or duty" created by the Exchange Act or its regulations—no matter how a plaintiff might characterize its claim—federal jurisdiction attaches and is exclusive. Neither prong of Section 27 turns on whether the Exchange Act itself creates the *claim* that is being asserted, and thus it is irrelevant whether the asserted claims purport to arise under state law. Indeed, the source of the asserted cause of action is irrelevant to Section 27's grant of federal jurisdiction.

A. The Third Circuit acknowledged below that all of Respondents' claims sought to establish a viola-

tion of, or enforce a duty created by, Regulation SHO, which imposes certain requirements on broker-dealers before they process short-sell orders. *See* App. 8a–9a; *see also id.* at 29a (same conclusion by district court). In fact, as the court noted, Respondents "repeatedly" alleged that Petitioners "violated" Regulation SHO. *Id.* at 8a–9a.[2] The Third Circuit nonetheless concluded that Section 27 "does not provide an independent basis to exercise [federal] jurisdiction," but instead merely "divest[s] state courts of jurisdiction" over claims within its scope. App. 22a. Thus, on the Third Circuit's view, the federal courts would have jurisdiction in this case only if there were some *other* basis—such as federal question—for exercising jurisdiction. *Ibid.*

The Third Circuit's decision cannot be reconciled with the text of Section 27, which expressly grants jurisdiction to federal courts rather than merely divesting jurisdiction from state courts: Section 27 unambiguously states that the federal courts "*shall have* exclusive *jurisdiction*" over the types of lawsuits covered by its terms. 15 U.S.C. § 78aa(a) (emphases added). This grant of authority is not negated merely because it is also exclusive. *See* Pet. Br. 29.

This textual reading is further strengthened by comparing Section 27 to Section 22 of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. § 77v. Both as originally enacted and as revised, Section 22 provides—just as Section 27 does with respect to the Exchange Act—that federal district courts "shall have

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[2] *Amici* take no position on the merits of the claims asserted or practices alleged below. *Amici* are solely interested in addressing issues raised by the Third Circuit's misinterpretation of Section 27.

jurisdiction" over claims alleging "violations" of the Securities Act or seeking to "enforce any liability or duty" that the Act creates. *See id.* § 77v(a); *see also* Securities Act of 1933, Pub. L. No. 73-22, § 22, 48 Stat. 74, 86.

This identical language is striking, but equally striking is the key difference: The word "exclusive" appears in Section 27 but not in Section 22. This should resolve the textual question in favor of Petitioners. As they correctly note, Section 22 is an affirmative grant of federal jurisdiction independent of federal-question jurisdiction under 28 U.S.C. § 1331. *See* Pet. Br. 30. Section 27 was adopted only one year later, by the same Congress. With jurisdictional language that differs only in its emphatic insistence on federal exclusivity, Section 27 cannot reasonably be interpreted to provide a *narrower*—indeed, on the Third Circuit's view, non-existent—grant of jurisdiction than Section 22. Moreover, the distinction between the two provisions with respect to exclusivity was not accidental; although Securities Act cases in many instances present no particular problems when litigated in state courts, the Exchange Act is predicated on the need for precision and national uniformity, thus making the need for exclusive federal jurisdiction imperative. *See infra* Part II.

B. The only inquiry necessary to determine whether a federal court has jurisdiction under Section 27 is whether the asserted claims (i) allege "violations of [the Exchange Act] or the rules and regulations thereunder," or (ii) seek to "enforce any liability or duty created by [the Exchange Act] or the rules and regulations thereunder." 15 U.S.C. § 78aa(a). Neither inquiry depends on what a plaintiff happens to *call* its claims, and neither depends on the label

(state or federal) attached to the relevant cause of action. Instead, Section 27 looks to what conduct the claims at issue challenge.

This point is illustrated most forcefully in lawsuits against SROs, which almost invariably implicate SROs' regulatory duties under the Exchange Act, the SEC's rules, or the SROs' own rules, and thus are subject to exclusive federal jurisdiction under Section 27.

Indeed, a reported Section 27 decision that does *not* involve an SRO is rare, as the bulk of the Section 27 cases cited in the certiorari-stage briefing in this Court illustrated. *See, e.g.*, Pet. 14–17; Opp. 23–26. In the context of such cases, the federal courts have repeatedly invoked Section 27 as a basis for federal jurisdiction—typically before dismissing the lawsuit at issue as barred by SROs' absolute immunity from claims challenging the exercise of their regulatory functions or by other federal doctrines (*e.g.*, the exclusivity of the Exchange Act's process for reviewing SRO actions). *See, e.g.*, *Sparta Surgical Corp.* v. *NASD*, 159 F.3d 1209, 1211–12 (9th Cir. 1998) (affirming denial of remand prior to dismissal); *Hawkins* v. *NASD*, 149 F.3d 330, 331–32 (5th Cir. 1998) (same); *see also, e.g.*, *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 98 (2d Cir. 2007) (Sotomayor, J.) (noting that SROs are immune where the "specific acts and forbearances" at issue "were incident to the exercise of regulatory power").[3] The Third Circuit

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[3] Decisions from the district courts are in accord. *See, e.g.*, *Lowe* v. *NASD Regulation*, No. 99-1751, 1999 WL 1680653, at *2–*4 (D.D.C. Dec. 14, 1999) (denying motion to remand); *Hibbard Brown & Co.* v. *NASD*, No. 94-285, 1994 WL 827778, at *2 (D. Del. Oct. 6, 1994) (same).

could not square its judgment with these cases, ultimately conceding that it simply "disagree[d]" with *Sparta* and *Hawkins*. *See* App. 20a & n.9.

In *Sparta*, a plaintiff brought purported state-law claims alleging that an SRO—the National Association of Securities Dealers ("NASD")—violated its own rules by suspending trading in two public offerings and delisting the shares. NASD's rules are promulgated under the Exchange Act, *see* 15 U.S.C. § 78s(b), and thus are "rules . . . thereunder" for purposes of Section 27. Because the lawsuit "sought relief based upon [alleged] violation of exchange rules," the Ninth Circuit held that "subject-matter jurisdiction was specifically vested in the federal district court under the Exchange Act." 159 F.3d at 1211.

Significantly, the Ninth Circuit noted that (as in this case) the claims at issue were "posited as state law claims." 159 F.3d at 1212. But they were nonetheless "founded on [NASD's] conduct in suspending trading and de-listing the offering, the propriety of which must be exclusively determined by federal law"—that is, the NASD's rules and the Exchange Act's detailed grant of authority to SROs—and thus "any claim falls under the imperative" of Section 27. 159 F.3d at 1212; *see also ibid.* ("The viability of any cause of action founded upon NASD's conduct in delisting a stock or suspending trading depends on whether the association's rules were violated.").

Similarly, in *Hawkins*, the plaintiff brought a state-law claim alleging that NASD violated "duties [that] arise from the NASD Code of Arbitration Procedure, which is a body of rules approved by the [SEC]." 149 F.3d at 331–32. The Fifth Circuit construed the plaintiff's attempt to enforce SRO rules as an "actio[n] at law seeking to enforce liabilities or

duties created by federal securities laws which are governed exclusively by federal courts." *Id.* at 332. Although the plaintiff's claims were "carefully articulated in terms of state law," the Fifth Circuit held that they fell within the exclusive jurisdiction of the federal courts because, *in substance*, they sought to "enforce liabilities or duties created by federal securities laws." *Ibid.*

* * *

Sparta and *Hawkins* illustrate two critical points that the Third Circuit missed. *First*, Section 27 is an affirmative grant of jurisdiction to the federal courts that is effective (and exclusive) regardless of whether federal jurisdiction might or might not exist under some other statute. *Second*, to determine whether Section 27 applies, the issue is not whether the cause of action sounds in federal law, but instead whether the claims allege "violations" of the Exchange Act or its regulations, or "seek to enforce rights or duties" that they create. This Court should endorse both propositions, and the Fifth and Ninth Circuit's analyses in *Sparta* and *Hawkins*, which together are sufficient to reverse the judgment below.

II. EXCLUSIVE FEDERAL JURISDICTION IS NECESSARY FOR EFFICIENT FUNCTIONING AND EFFECTIVE REGULATION OF THE NATION'S SECURITIES MARKETS.

As with other comprehensive federal regulatory systems,[4] this Court has recognized that the Ex-

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[4] *See, e.g., United States* v. *Locke*, 529 U.S. 89, 97 (2000) (maritime vessels); *Bonito Boats, Inc.* v. *Thunder Craft Boats, Inc.*, 489 U.S. 141, 162–63 (1989) (patent law); *Rogers' Estate* v. *Helvering*, 320 U.S. 410, 414 (1943) (federal taxation).

change Act—and Section 27 in particular—are intended "to achieve greater uniformity of construction and more effective and expert application of that law." *Matsushita Elec. Indus. Co.* v. *Epstein*, 516 U.S. 367, 382 (1996). These objectives would be difficult, if not impossible, to achieve without the exclusive federal jurisdiction that Section 27 creates.

A. SROs Play A Key Role In Securities Trading And Regulation.

The Exchange Act creates "a detailed, comprehensive system of federal regulation of the securities industry" founded on "self-regulation by industry organizations." *Swirsky* v. *NASD*, 124 F.3d 59, 61 (1st Cir. 1997). This "regulatory model" depends, in part, on the "delegation of certain government functions to private SROs," *In re Series 7 Broker Qualification Exam Scoring Litig.*, 548 F.3d 110, 114 (D.C. Cir. 2008), which "serv[e] as a critical aid to the SEC in implementing and effectuating compliance with the securities laws," *DL Capital Group* v. *NASDAQ Stock Market*, 409 F.3d 93, 95 (2d Cir. 2005).

1. SROs are private, non-governmental organizations that have the power to create and enforce industry regulations and standards. They have long played an important role in securities markets and securities regulation. In 1792, the New York broker community formed the first organized stock market (*viz.*, NYSE). *See Concept Release Concerning Self-Regulation* ("*Concept Release*"), SEC Release No. 34-50700, 69 Fed. Reg. 71,256, 71,257 (Dec. 8, 2004). As NYSE and other stock exchanges developed, trading conventions became formalized as exchange rules. *Ibid.*

Federal regulation of SROs began in 1934 with the Exchange Act, which required exchanges to reg-

ister with the SEC and to function as SROs. *See Concept Release*, 69 Fed. Reg. at 71,257. In 1938, the Maloney Act amended the Exchange Act to allow the formation of non-exchange SROs, which led to the creation of NASD (now known as the Financial Industry Regulatory Authority) and the National Futures Association. *See ibid.*

As securities trading developed, and in an attempt to increase the fairness, competitiveness, and efficiency of U.S. securities markets, Congress passed the Exchange Act Amendments of 1975. *See* SEC, Division of Market Regulation, *Market 2000: An Examination of Current Equity Market Developments* ("*Market 2000*") at I-3–I-5 (Jan. 1994), *at* https://www.sec.gov/divisions/marketreg/market2000.pdf. The 1975 Amendments provided a new framework for a national market system and, while reiterating Congress's commitment to self-regulation, granted the SEC significantly broader oversight power over SROs. *See Market 2000* at I-4–I-5.

As the SEC has observed, the Exchange Act, the Maloney Act, and the 1975 Amendments "reflect Congress' determination to rely on [SROs] as a fundamental component of U.S. market and broker-dealer regulation" for at least three reasons. *Concept Release*, 69 Fed. Reg. at 71,256. *First*, it was far more cost-effective for SROs to "effectively regulat[e] the inner-workings of the securities industry." *Ibid. Second*, "the complexity of securities trading practices made it desirable for SRO regulatory staff to be intimately involved with SRO rulemaking and enforcement." *Ibid. Third*, "the SROs could set standards that exceeded those imposed by the Commission, such as just and equitable principles of trade

and detailed proscriptive business conduct standards." *Ibid.* Congress thus determined that, without SROs and their important function in providing standardized and predictable governance, fair and efficient securities regulation would not be possible.

2. SROs are responsible for promulgating and enforcing rules that govern all aspects of their members' securities business, including their financial condition, operational capabilities, sales practices, and qualifications of their personnel. *See, e.g.*, 15 U.S.C. §§ 78f(b), 78*o*-3(b), 78s(b). With few exceptions, the SEC must approve all SRO rules, policies, practices, and interpretations before they are implemented. *See id.* § 78s(b). And because SRO rules are approved by the SEC, those rules share the preemptive effect of other federal regulations. *See Credit Suisse First Boston Corp.* v. *Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005). The SEC is also empowered to "abrogate, add to, and delete from" SRO rules "as the Commission deems necessary or appropriate." 15 U.S.C. § 78s(c); *see generally, e.g.*, *Shearson/Am. Express Inc.* v. *McMahon*, 482 U.S. 220, 233–34 (1987) (describing the SEC's authority to approve, disapprove, or modify SRO rules).

In fulfilling their regulatory functions, SROs also conduct investigations and examinations at their members' premises, monitor financial and other operational reports, investigate potential rule violations, and bring disciplinary proceedings when appropriate. *See Concept Release*, 69 Fed. Reg. at 71,261. In addition, SROs monitor trading on the markets they operate to detect evidence of rule violations and other improper practices, such as insider trading and market manipulation. *Ibid.*

With respect to each of these SRO activities, the SEC's review authority is comprehensive. The SEC is authorized to review actions taken by SROs "on its own motion, or upon application by any person aggrieved thereby." 15 U.S.C. § 78s(d)(2). In this way, and through its power over the creation and modification of SRO rules, the SEC provides significant—and uniform—oversight of SROs. The goal of this process, as Congress intended, is fair treatment of investors and fair competition among markets and market participants. *See id.* § 78f(b)(5).

B. Exclusive Federal Jurisdiction Provides Uniformity That Is Necessary For SROs To Function Effectively.

The absence of an SRO as a party makes this an unusual reported Section 27 decision. Given their centrality to securities regulation and their prominent role within the Exchange Act in particular, SROs are almost universally among the parties to suits generating reported decisions on Section 27. Indeed, the three other cases that comprise the circuit split invoked by Petitioners in this case all involved lawsuits against SROs. *Compare Barbara* v. *NYSE*, 99 F.3d 49 (2d Cir. 1996), *with Hawkins*, 149 F.3d 330, *and Sparta*, 159 F.3d 1209. It is precisely that context that illustrates most clearly the importance of uniform administration and interpretation of the Exchange Act, the SEC's rules, and SRO rules, which Section 27 provides as properly construed.

1. Uniformity is critical because SROs must be nimble, which is possible only if they can make regulatory decisions and respond to changing market conditions without fear that their actions will be

judged under varying and unpredictable standards in different states. *See, e.g.*, *DL Capital*, 409 F.3d at 99 (cautioning against "disruptive and recriminatory lawsuits" that would "unduly hampe[r]" SROs' "quasi-governmental functions"). Indeed, Congress included SROs as part of the Exchange Act's regulatory regime because of their unique ability to bring the "informality and flexibility of self-regulatory procedures" into complex, ever-changing securities markets. S. Doc. No. 93-13, at 149 (1973). SROs can fulfill that function only because the system of exclusive regulation by the SEC and federal courts provides them with clear and uniform guidance on the proper use and limits of their power.

This regulatory system has given rise to a robust body of federal case law that provides predictable means to resolve complaints against SROs. Federal courts have applied the doctrines of regulatory immunity and exclusive federal review to safeguard SROs' independent regulatory judgments from second-guessing by dissatisfied market participants. *See, e.g.*, *Series 7*, 548 F.3d at 115 ("Congress did not intend the regulatory duties at issue here to be enforced by common law causes of action."); *Sparta*, 159 F.3d at 1215 (rejecting a "theory [that] would allow states to define by common law the regulatory duties of a self-regulatory organization").

Similarly, the federal courts' insistence that plaintiffs pursue administrative remedies before the SEC has reinforced the centralized, expert system of SRO regulation created by Congress. *See, e.g.*, *Series 7*, 548 F.3d at 114 (holding that "[t]he multiple layers of review" for SRO actions "evince Congress's intent to direct challenges . . . to the avenues Congress created"); *see also Altman* v. *SEC*, 687 F.3d 44, 46 (2d

Cir. 2012) (per curiam) (holding that the Exchange Act's review process "suppl[ies] the jurisdictional route that [litigants] must follow to challenge" actions subject to that process).

Fidelity to these doctrines in federal court has ensured that SROs maintain the discretion and flexibility required to regulate and operate the markets and that the Exchange Act's promise of uniform, expert regulation of the securities markets remains fulfilled. Indeed, the existence of a coherent body of federal law interpreting these doctrines, the Exchange Act, and the SEC's regulations provides SROs with the predictable framework that they need to undertake their critical function.

2. Discarding this uniformity in favor of a state-by-state approach to interpretation of the Exchange Act, SEC rules, and SRO rules would wreck this carefully calibrated system. SROs would, in effect, acquire scores of new regulators, with each state being able to offer its own interpretation of SROs' rules and duties. With so many jurisdictions putting their own glosses on the Exchange Act and the rules promulgated thereunder, conflicting judicial mandates become practically inevitable. The mere *possibility* of these results is enough to destroy the vital predictability and certainty that Congress sought to provide through access to the federal court system. *See, e.g.*, *Sparta*, 159 F.3d at 1215 (noting that state-by-state regulation of SROs "cannot co-exist with the Congressional scheme of delegated regulatory authority under the Exchange Act").

The patchwork regulatory system that would follow from the decision below would, therefore, threaten SROs' abilities to perform their core functions under the Exchange Act. Simply monitoring the devel-

opments across fifty or more jurisdictions would impose enormous new burdens on SROs; attempting to comply with all of the ever-changing and overlapping rulings would be virtually impossible. SROs would lose their unique ability to respond quickly and decisively to changing market conditions. And the Exchange Act's vision of a uniform, national system of securities-markets regulation would be destroyed.

3. This Court has already recognized the significance of these concerns. Explaining the reasons behind the preemptive effect of the securities laws, the Court highlighted the dangers of permitting varying interpretations in state courts across the country: "[P]laintiffs may bring lawsuits throughout the Nation in dozens of different courts with different nonexpert judges and different nonexpert juries. . . . [I]t will prove difficult for those many different courts to reach consistent results." *Credit Suisse Sec. (USA) LLC* v. *Billing*, 551 U.S. 264, 281 (2007).[5] The Court rejected the imposition of antitrust law into the collective-bargaining context for similar reasons, decrying the resulting "web of detailed rules spun by many different nonexpert antitrust judges and juries" that would replace the uniform "set of . . . rules enforced by a single expert administrative body." *Brown* v.

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[5] As Petitioners note, state courts have in rare instances purported to exercise jurisdiction over Section 27 cases. *See* Pet. Br. 25 n.8. Those cases provide no support for disregarding Section 27's express grant of "exclusive" federal jurisdiction, and in any event simply demonstrate why Congress found it essential to limit jurisdiction to the federal courts. *See* Pet. Br. 25 n.8; *see also, e.g.*, *Platinum Partners Value Arbitrage Fund, Ltd. P'ship* v. *Chi. Bd. Options Exch.*, 976 N.E.2d 415 (Ill. Ct. App. 2012) (state court decision at odds with federal jurisprudence involving SROs).

Pro Football, Inc., 518 U.S. 231, 242 (1996); *see also, e.g., United States* v. *NASD*, 422 U.S. 694, 729–30 (1975) (holding that "the antitrust laws must give way if the regulatory scheme established by the Investment Company Act is to work").

These concerns apply with greater force here. Indeed, given the technical subject matter and the heightened need for uniform regulation of SROs, Congress saw fit to exclude even federal district courts from the regulatory process in most instances. The Exchange Act channels complaints over SROs' decisions through the SEC to ensure expert interpretation of these technical statutes and regulations. *See* 15 U.S.C. § 78s(a)-(d), (g)-(h). From there, the Exchange Act funnels complaints about the SEC's decision not to a federal district court (or, as Respondents wish here, a state trial court), but to a federal court of appeals. *See id.* § 78y(a)(1); *see also, e.g., Series 7*, 548 F.3d at 114; *Altman*, 687 F.3d at 46. In a comprehensively crafted system that displaces trial court litigation in most circumstances, and channels litigation exclusively through the federal courts, the threat to uniformity that necessarily would flow from the Third Circuit's interpretation of Section 27 would be especially egregious. This Court should refuse to permit such a result.

* * *

For all of these reasons, Congress focused on the overriding need for centralized, uniform interpretation of the Exchange Act and its accompanying regulations when it enacted Section 27: "[T]he exclusive-federal-jurisdiction provision in the 1934 act was motivated by a desire to achieve a greater uniformity of construction . . . than would be possible if the many state courts were to be kept in line only through the

Supreme Court's certiorari jurisdiction." Louis Loss, *The SEC Proxy Rules and State Law*, 73 Harv. L. Rev. 1249, 1275 (1960). This Court should recognize the good sense of that approach and honor the statute's text, which (as discussed above) plainly codifies Congress's vision of uniform federal interpretation of the Exchange Act and the rules thereunder.

III. THE SECOND CIRCUIT'S MORE RECENT OPINIONS HAVE CALLED INTO QUESTION ITS ERRONEOUS DECISION IN *BARBARA* V. *NEW YORK STOCK EXCHANGE*.

Because the plain text and overriding objectives of Section 27 unambiguously demonstrate that the statute confers exclusive federal jurisdiction, all that remains of the Third Circuit's contrary analysis is its heavy reliance on the Second Circuit's decision in *Barbara*. But *Barbara* was incorrectly decided, predated *Sparta* and *Hawkins*, and in any event has subsequently been narrowed within the Second Circuit itself. The Third Circuit's reliance on *Barbara* for its Section 27 analysis only further demonstrates the infirmity of the judgment below.

A. The facts of *Barbara* were straightforward. The plaintiff worked as a "floor clerk" at different NYSE member firms, and thus was given access to NYSE's floor pursuant to NYSE's rules. 99 F.3d at 51–52. This changed, however, when the plaintiff was investigated by NYSE's enforcement arm and, during the course of the investigation, was barred from the exchange floor. *Ibid.* Although this disciplinary action was eventually reversed by NYSE's board of directors, the experience effectively ended the plaintiff's career. *Ibid.*

The jurisdictional issue arose when the plaintiff filed suit in New York state court, alleging various

state-law causes of action on the theory that NYSE "had wrongfully barred him from the Exchange floor, thereby damaging [his] reputation and causing him to lose employment opportunities." 99 F.3d at 52. NYSE removed the case to federal court, and the plaintiff did not challenge removal. *Ibid.* NYSE moved to dismiss the complaint, arguing (among other things) that the lawsuit was barred by SROs' absolute immunity for their regulatory actions. The plaintiff sought leave to file an amended complaint before NYSE had filed its responsive pleading; the proposed amended complaint added claims that NYSE denied him due process in violation of the Fifth Amendment to the United States Constitution and 42 U.S.C. § 1983. The district court granted NYSE's motion to dismiss and denied as moot the plaintiff's motion to amend. 99 F.3d at 53.

On appeal, the Second Circuit considered federal jurisdiction *sua sponte*, and stated that the district court lacked jurisdiction over the plaintiff's original complaint. 99 F.3d at 53-56. None of the jurisdictional issues—in particular, those at issue here—had been addressed in the parties' briefs.

First analyzing the original complaint under 28 U.S.C. § 1331, the court noted that each claim was asserted under state law and that any federal issues—including SRO immunity—were defenses and thus could not by themselves create federal jurisdiction, *see* 99 F.3d at 53.

The Second Circuit then considered whether jurisdiction was appropriate under the rule providing federal jurisdiction where "the plaintiff's right to relief under state law necessarily depends on resolution of a substantial question of federal law." 99 F.3d at 54 (citation and alteration omitted). As the court

acknowledged, the plaintiff's "state court complaint [did] make factual allegations that the [NYSE] violated . . . internal rules" that it had established pursuant to the Exchange Act and under the SEC's supervision. *Ibid.*

According to the Second Circuit, however, this federal nexus was insufficient to warrant federal jurisdiction for two reasons. *First*, the Exchange Act lacks a private right of action to enforce NYSE rules, which—despite detailed provisions in the Exchange Act governing review of those rules, *see* 15 U.S.C. §§ 78s(b) (SEC review), 78y(a)(1) (subsequent review by a court of appeals)—the Second Circuit (incorrectly) understood to mean that federal law could not have created the rule of decision for the plaintiff's claims. 99 F.3d at 54. *Second*, the Second Circuit believed that NYSE's rules were "contractual in nature . . . and are thus interpreted pursuant to ordinary principles of contract law, an area in which the federal courts have no special expertise." *Id.* at 54–55 (citation omitted).

Finally, the Second Circuit rejected Section 27 as an independent basis for jurisdiction. The court stated that its "determination that [the plaintiff's] state court complaint did not 'arise under' federal law within the meaning of section 1331 effectively resolve[d] [its] inquiry under section 27 of the Exchange Act as well." 99 F.3d at 55. According to the court, Section 27's text "plainly refers to claims created by the [Exchange] Act or by rules promulgated thereunder, but not to claims created by state law." *Id.* at 55. Thus, the court largely merged the inquiries under federal-question jurisdiction and Section 27, and did not meaningfully analyze or even discuss the terms of Section 27.

B. As an initial matter, *Barbara*'s discussion of jurisdiction over the plaintiff's *original* complaint was unnecessary and thus *dicta*. Following that discussion, the court addressed the import of the plaintiff's proposed *amended* complaint. That pleading plainly would have given the district court jurisdiction because the plaintiff sought to amend his complaint to add claims that were *expressly federal*, "thereby conferring subject matter jurisdiction upon the federal courts." 99 F.3d at 56. There was, accordingly, no need to reach out and decide a jurisdictional question that was self-evidently and immediately mooted by the amended complaint.

Having found jurisdiction through the amended complaint, the Second Circuit then affirmed the district court's judgment of dismissal because the disciplinary proceedings at issue were part of NYSE's "official duties" for which it had absolute immunity from suit. *Id.* at 58–59.

C. Moreover, the Second Circuit's subsequent case law has significantly narrowed *Barbara*'s jurisdictional *dicta* and cast grave doubt on its logic.

D'Alessio v. *NYSE*, 258 F.3d 93 (2d Cir. 2001), provided the Second Circuit's initial step back from *Barbara*'s *dicta*. In *D'Alessio*, the plaintiff—as in *Barbara*—had been suspended from NYSE's floor and sued NYSE in state court for state-law claims arising out of the suspension and related enforcement proceedings. NYSE removed the case to federal court, and the district court eventually dismissed the case with prejudice based on *Barbara*'s absolute-immunity ruling. *Id.* at 98.

On appeal, the Second Circuit again considered its jurisdiction *sua sponte*, and concluded that it had jurisdiction. Following an extended discussion of

Barbara, the court of appeals sought to distinguish *Barbara*'s *dicta*. According to *D'Alessio*, *Barbara* concerned only NYSE's application of its own supposedly contract-like rules, whereas the plaintiff in *D'Alessio* had alleged that NYSE violated not only its own rules, but also "the federal securities laws and various rules promulgated by [NYSE] and failed to perform its statutory duty, *created under federal law*, to enforce its members' compliance with those laws." 258 F.3d at 101.

But *D'Alessio* did not explain how this observation could distinguish the NYSE rules at issue in *Barbara*, which *Barbara* acknowledged *also* were established pursuant to the federal securities laws. *Barbara*, 99 F.3d at 54. And—without even acknowledging *Barbara*'s *dicta* that Section 27 does not provide an independent basis for federal jurisdiction—*D'Alessio* cited Section 27's exclusive jurisdiction as a "recognition" of the "importance of federal regulation of the stock market." 258 F.3d at 104 (citation omitted).

The Second Circuit's effective repudiation of *Barbara*'s jurisdictional *dicta* continued last year in *NASDAQ OMX Group* v. *UBS Securities, LLC*, 770 F.3d 1010 (2d Cir. 2014). In *UBS*, the plaintiff had initiated arbitration against NASDAQ pursuant to a clause in NASDAQ's service agreement, seeking damages under four state-law claims resulting from complications in Facebook's initial public offering. *Id.* at 1013–17. NASDAQ sued in federal court to enjoin the arbitration and for a declaratory judgment of immunity from suit. The district court issued a preliminary injunction, and the plaintiff appealed.

The Second Circuit relied on the four-part test for federal-question jurisdiction articulated in *Grable*

& Sons Metal Products, Inc. v. *Darue Engineering & Manufacturing*, 545 U.S. 308 (2005), and *Gunn* v. *Minton*, 133 S. Ct. 1059 (2013)—that is, whether the federal issue is "(1) necessarily raised, (2) actually disputed, (3) substantial, and (4) capable of resolution in federal court without disrupting the federal-state balance." *Gunn*, 133 S. Ct. at 1065. The Second Circuit concluded that the federal interests involved supported jurisdiction, and articulated a rule that could grant federal jurisdiction over nearly every claim related to the functioning of a stock exchange and its compliance with the regulatory regime superintended by the SEC. *UBS*, 770 F.3d at 1020–31.[6]

The federal issue raised and disputed was whether NASDAQ had satisfied its statutory obligation "to operate a fair and orderly market," 770 F.3d at 1021—an obligation created by the Exchange Act that would also cover investigation and discipline of the floor clerk in *Barbara*. The federal-state balance would not be disturbed because, according to the court, Section 27 demonstrated that Congress intended federal courts to adjudicate securities matters. *Id.* at 1030–31. As for "substantiality," the court of appeals identified simply "the central role stock exchanges play in the national system of securities markets." *Id.* at 1024.

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[6] This Court is not presented with the question whether Section 1331, under the *Grable-Gunn* analysis, would support federal jurisdiction in this case. Rather, the question presented is limited to whether Section 27 confers federal jurisdiction. Accordingly, this Court need not address *other* potential grounds for jurisdiction, such as Section 1331. *See, e.g.*, *UBS*, 770 F.3d at 1020–31.

Regarding this final category, the Second Circuit reconsidered *Barbara*'s essential premise: that SRO rules are supposedly "'contractual in nature'" and thus have little federal interest. 770 F.3d at 1025 (quoting *Barbara*, 99 F.3d at 54–55). The court correctly noted that *Barbara* had ignored the importance of SEC approval of SRO rules, which itself created a substantial federal interest in adjudicating alleged violations of those rules. *Id.* at 1026. The court explained away this oversight by emphasizing the "trifling significance" of the dispute in *Barbara*. *Ibid.* Notwithstanding *Barbara*'s logical shortcomings, as noted by the *UBS* court, *UBS* did not revisit *Barbara*'s *dicta* that Section 27 does not grant jurisdiction because the *Grable-Gunn* jurisdictional test had achieved the same result. *Id.* at 1030–31.

* * *

Whatever merit *Barbara*'s jurisdictional *dicta* might have had as originally decided—and the discussion above makes clear that it had none—the decision has been thoroughly undermined by subsequent decisions, and thus should have no persuasive force in this Court. Instead, this Court should rely on the plain text of Section 27 and the reasoning of cases applying the plain text, like *Sparta* and *Hawkins*, to hold that Section 27 is an affirmative and exclusive grant of jurisdiction that turns solely on whether the claims at issue satisfy one of the statute's two prongs, both of which are independent of the source of the cause of action or "state-law" label invoked by the plaintiff.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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